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September 13, 2019

VIA ELECTRONIC DELIVERY

The Honorable Jocelyn G. Boyd
Chief Clerk/Administrator
Public Service Commission of South Carolina
101 Executive Center Drive
Columbia, South Carolina 29210

RE: Dominion Energy South Carolina, Inc.'s Filing of Quarterly Monitoring Report for the twelve-month period ending March 31, 2019, and Proposed Rate Adjustments Pursuant to the Natural Gas Rate Stabilization Act
Docket No. 2019-6-G

Dear Ms. Boyd:

Enclosed on behalf of Dominion Energy South Carolina, Inc. ("DESC" or the "Company") you will find the Company's Response to the South Carolina Office of Regulatory Staff's ("ORS") Review of DESC's Gas Rate Stabilization Act Monitoring Report in the above-captioned matter.

By copy of this letter we are serving the South Carolina Office of Regulatory Staff with a copy of the enclosed documents and attach a certificate of service to that effect.

If you have any questions, please advise.

Very truly yours,

Matthew W. Gissendanner

Matthew W. Gissendanner

MWG/kms
Enclosure

cc: Andrew M. Bateman, Esquire
Jenny R. Pittman, Esquire
(via electronic mail and First Class U.S. Mail w/enclosures)

BEFORE

THE PUBLIC SERVICE COMMISSION

OF

SOUTH CAROLINA

DOCKET NO. 2019-6-G

Dominion Energy South Carolina, Inc.'s Filing of Quarterly Monitoring Report for the twelve-month period ending March 31, 2019, and Proposed Rate Adjustments Pursuant to the Natural Gas Rate Stabilization Act	)))))))	**DOMINION ENERGY SOUTH CAROLINA, INC.'S RESPONSE TO OFFICE OF REGULATORY STAFF'S REVIEW OF DOMINION ENERGY SOUTH CAROLINA, INC.'S GAS RATE STABILIZATION ACT MONITORING REPORT**

Dominion Energy South Carolina, Inc. ("DESC" or the "Company")[1] provides these comments to the Public Service Commission of South Carolina ("Commission") pursuant to S.C. Code Ann. §§ 58-5-400 *et seq.* (2015, as amended), the Natural Gas Rate Stabilization Act ("Act"). These comments are provided in response to the Review of Dominion Energy South Carolina, Inc.'s Gas Rate Stabilization Act Monitoring Report for the period ending March 31, 2019, (the "Report") issued by the Office of Regulatory Staff ("ORS").

For purposes of this proceeding, DESC does not contest any elements of the Report except the 1) disallowances related to economic development expenses; 2) reduction of employee incentive pay; and 3) removal of fifty percent of the base pay and benefits paid to the Company's four executives with the highest amount of compensation allocated to South Carolina natural gas operations. As explained below, DESC believes these items are appropriate for inclusion in gas

[1] South Carolina Electric & Gas Company ("SCE&G") changed its name to Dominion Energy South Carolina, Inc. effective April 29, 2019. This Response uses "DESC" to refer to the Company both before and after this name change.

rates and should not be disallowed. DESC respectfully requests the Commission allow DESC to recover the amount of these proposed disallowances, totaling $601,456.

DESC limits its comment to these three items without conceding that any other disallowances or reductions in the ORS Report are proper and without waiving any arguments challenging disallowance of any other items. Further, DESC refers the Commission and all parties to Docket No. 2019-232-A, Procedure to Address Conceptual Issues Around Non-Allowable Expenses (See Page Number 4 of Order No. 2019-341), and DESC's comments filed in that docket. DESC does not waive any of the arguments it made in Docket No. 2019-232-A.

PROCEDURAL STATEMENT

Under the terms of S.C. Code Ann. § 58-5-455, on or before June 15th of each year, the Company files a Rate Stabilization Act ("RSA") monitoring report with the Commission and ORS for the 12-month period ending March 31st. Interested parties may comment on the reports. S.C. Code Ann. § 58-5-455. Where it appears to the Commission or ORS that an adjustment in rates may be warranted, the statute requires that ORS conduct an audit of the monitoring report and specify any changes that it determines are necessary to correct errors in the report or to otherwise bring the report into compliance with the Act. *Id.* Interested parties may then file comments on the ORS Report and the audit findings and recommendations it contains. *Id.* On or before October 15th, the Commission issues an initial order setting forth any changes required in the utility's request to adjust rates under the statute as provided by S.C. Code Ann. § 58-5-455(5). Any rate adjustment authorized under the terms of the statute takes effect for bills rendered on or after the first billing cycle of November of that year. *Id.*

On June 14, 2019, DESC submitted its quarterly monitoring report for the twelve-month period ending March 31, 2019. Order No. 2005-619, issued in Docket No. 2005-113-G, authorized a 10.25% return on common equity for the Company, which is the baseline return on equity for the Company under the Act. *See also* Order No. 2006-553, dated September 27, 2006, in Docket No. 2006-157-G. DESC's 2019 report showed that an increase in revenue of $7,106,649 is required to restore its return on common equity to 10.25% as specified in Order No. 2005-619. This follows a decrease in revenue of ($19,716,936), which was ordered in the 2018 RSA review. *See* Order No. 2018-678 at 2.

As required by S.C. Code Ann. § 58-5-450, ORS reviewed the monitoring report for the twelve-month period ending March 31, 2019, and evaluated compliance with the reporting provisions contained in Section 58-5-430 and Section 58-5-440 of the Act. In its Report, the ORS proposed certain adjustments and calculated the as-adjusted rate of return and return on common equity for DESC to be 7.32% and 8.78%, respectively.

Accordingly, ORS recommended that the Commission authorize an increase in DESC's gas revenues of $6,273,054. This amount reflects an adjustment by ORS to the Company's request of ($833,595). ORS states that, after the proposed decrease, the Company will have an opportunity to earn a rate of return and return on common equity of 8.04% and 10.25%, respectively.

LEGAL STANDARDS

The overarching legal standard for utility rates is that they must be "just and reasonable." S.C. Code Ann. § 58-27-810. This standard incorporates the rule that unjust or insufficient rates constitute a taking of private property for public use without just compensation in violation of the Takings Clause of the United States and South Carolina Constitutions. U.S. Const. amend. V; S.C. Const. art. I, § 13(A); *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 308 (1989); *accord, S. Bell Telephone & Telegraph Co. v. S.C. Pub. Serv. Comm'n*, 270 S.C. 590, 595-96, 244 S.E.2d 278, 281 (1978).

In the seminal case of *Federal Power Comm'n v. Hope Natural Gas Co.*, the United States Supreme Court recognized the link between expenses and compensatory returns: In setting a just and reasonable rate "it is important that there be enough revenue ***not only for operating expenses*** but also for the capital costs of the business." *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (emphasis supplied). The failure to acknowledge a significant known and measurable expense item is reversible error. *Daufuskie Island Util. Co., Inc. v. S.C. Office of Regulatory Staff*, 420 S.C. 305, 318–19, 803 S.E.2d 280, 287 (2017). In setting rates under the Act, the Commission is charged with recognizing

> all applicable accounting and pro-forma adjustments historically permitted or required by the commission for the utility in question, or for similarly situated utilities, or authorized by general principles of utility accounting, or authorized by accounting letters or orders issued by the commission. This authorization may occur either in a general rate hearing or in any other type of filing or hearing that the commission considers appropriate.

S.C. Code Ann. § 58-5-430.

The disallowances made by ORS in the Report fail to meet these standards. As discussed more fully below, none of the three adjustments comport with general principles of utility accounting or sound rate making policies because they deny the Company the opportunity to recover reasonable and appropriate costs of managing its utility system for the benefit of customers. In addition, the proposed disallowances related to (1) economic development expenses and (2) base pay and benefits paid to the four executives with the highest amount of compensation allocated to South Carolina natural gas operations are outside of the scope of pro forma adjustments historically recognized for the Company. These expenses have been routinely allowed in past cases.

The disallowances related to the reduction of employee incentive pay are outside of the pro forma adjustments approved by the Commission for similarly situated utilities. *See* Order No.

2019-341 at 107, Docket No. 2018-318-E; Order No. 2019-323 at 27, 56-57, Docket No. 2018-319-E. In those cases, the Commission did not adopt identical adjustments recommended by ORS for Duke Energy Carolinas, LLC and Duke Energy Progress, LLC.

ARGUMENT

As discussed below, each of the three challenge disallowances involves reasonable and appropriate costs of managing a utility system and is outside of the scope of the adjustments authorized by S.C. Code Ann. § 58-5-430.

1. Disallowances Related to Economic Development

ORS seeks to disallow $34,501 for "development grants and sponsorships" asserting that the costs "do not directly relate to the provision of safe and reliable gas operations or increase total system sales and customers." ORS Report at 3-4. The economic development expenses ORS proposes to disallow are:

- **Dorchester County** – Grant for Dorchester County Economic Development to purchase the Pine Hill Business Campus, a 330-acre industrial park, to preserve the land for industrial use. **(Sample #131, Gas Amount $27,330.00)**
- **Economic Leadership Council** – Hotel expense for the Senior Vice President of Governmental Affairs and Economic Development (at the time) to attend the Economic Leadership Council Meeting in Charleston, South Carolina. **(Sample #190, Gas Amount $13.89)**
- **Charleston Regional Development Alliance (CRDA)** - Annual operating support for CRDA economic development activities, assisting businesses and entrepreneurs locating and expanding in the greater Charleston area, which includes Berkeley, Charleston and Dorchester counties. CRDA also streamlines the site selection process, assisting with talent, buildings and sites, financing, and workforce training needs. **(Sample #204, Gas Amount $3,924.00)**
- **South Carolina I-77 Alliance** - Annual operating support for the I-77 Alliance which markets the business and manufacturing opportunities throughout a diverse five-county area known as the "I-77 Corridor" that stretches from Columbia, SC to just south of Charlotte, NC. Also help create lead generation, marketing and branding for the area. **(Sample #205, Gas Amount $1,502.50)**
- **Southern Carolina Alliance** - Annual support for economic development and industrial recruitment activities conducted by the Southern Carolina Alliance in Allendale, Bamberg,

Barnwell, Beaufort, Hampton, Colleton and Jasper Counties. **(Sample #206, Gas Amount $601.00)**

- **Marlboro County Economic Development Partnership** - Annual support for the Marlboro County's economic development organization. **(Sample #207, Gas Amount $500.00)**
- **Economic Development Partnership Inc. (EDIP)**- Annual operating support for the EDPI, a non-profit public-private development corporation focused solely on serving the needs of new and existing businesses in the Aiken, Edgefield, McCormick, and Saluda Region of South Carolina. **(Sample #208, Gas Amount $300.50)**
- **South Carolina Economic Developers Association (SCEDA)** – Annual support for SCEDA (which provided two memberships) and six additional memberships for DESC employees. SCEDA's mission to advocate for economic development in South Carolina and enhance the professional development of the membership. Members come from all 46 Counties and include local and regional economic developers, as well as officials from municipal, county and state government agencies, construction and engineering firms, utility companies, attorneys, consultants, financial institutions, and higher education. **(Sample #209, Gas Amount $240.40 and Sample #210, Gas Amount $72.12)**
- **Dillon County Public – Private Economic Development Partnership** - Annual membership for Dillon County's economic development organization. **(Sample #211, Gas Amount $9.02)**
- **Marion County Progress Inc.** - Annual support for Marion County's economic development efforts. **(Sample #212, Gas Amount $7.51)**

Economic development benefits customers. It ensures continued growth and expansion of the gas system in the state, which benefits customers generally by providing jobs and economic activity that promote prosperity in the service territory and more specifically by expanding the natural gas through-put over which to spread the costs of the distribution system. Industrial gas users make a substantial contribution to system economics and are often high-volume, high-load factor customers, which benefit system operations and lower rates to other customers. Industrial development projects generate spin off businesses and development which multiplies the impact of the direct contributions made.

Certain of the economic development costs in question here are modest amounts of annual support given to local and regional economic development programs across the state. These amounts are highly leveraged by being combined with the support from other members and the state and local funding sources available to these programs.

Similar expenditures have been accepted in previous RSA and other filings as valid expenses of utility operations. Nothing has been produced here to explain why a different policy should apply to these expenses. Multiple accounting orders have recognized the recoverability of such expenses. *See, e.g.,* Order No. 2012-662 (granting an accounting order deferring for future recovery an economic development grant to the Aiken County); Order No. 2011-510 (granting an accounting order deferring for future recovery an economic development grant to the Central SC Alliance); Order No. 2009-907 (granting an accounting order deferring for future recovery an economic development grant to Barnwell County). DESC respectfully requests the Commission allow recovery of the $34,501 of costs associated with economic development matters. Under S.C. Code Ann. § 58-5-430, the recommended adjustment to disallow these costs is clearly not an "accounting and pro-forma adjustments historically permitted or required by the commission for the utility in question, or for similarly situated utilities, or authorized by general principles of utility accounting, or authorized by accounting letters or orders issued by the commission." S.C. Code Ann. § 58-5-430.

2. Employee Incentive Pay

ORS recommends an adjustment of $237,172 to remove the portion of Long-Term Incentives and Short-Term Incentives for the Company's Earnings per Share and Total Shareholder Return goals. DESC respectfully submits that these costs are valid and appropriate costs of utility operations and should be allowed.

DESC's position in this docket is consistent with the Order in the most recent Duke Energy Progress, LLC and Duke Energy Carolinas, LLC electric rate proceedings. In those proceedings, the Commission authorized Duke Energy Progress and Duke Energy Carolinas to recover 100% of its incentive compensation to employees through rates. *See* Order No. 2019-341 at 107, Docket No. 2018-318-E; Order No. 2019-323 at 27, 56-57, Docket No. 2018-319-E.

As the Commission explained, "[t]he incentive compensation which the ORS seeks to disallow is a prudently incurred cost of service which comprises only a portion of overall employee compensation expense." Order No. 2019-323 at 27. The Commission recognized that "[i]ncentive compensation, particularly that of non-executive-level employees, is merely a portion of overall employee compensation expense and a prudently incurred cost of service." *Id.* at 56. Incentive compensation is nothing more than a managerial decision as to how to pay employees, and there is no basis for which to reject compensation of employees generally. *See id.*

DESC affirms the logic and reasoning behind this decision. The Commission's decision in the Duke proceedings is fully consistent with the testimony DESC provided in its last retail electric rate proceeding, Docket No. 2012-218-E. That testimony explained that "incentive compensation is an integral part of [DESC's] total compensation package for its employees." Order No. 2012-951 at 27. It showed that "incentive compensation is an important tool that the Company uses to communicate key goals and business objectives to employees in a way that motivates employees to embrace them and become accountable for accomplishing them." *Id.* at 28. The Commission accepted that testimony "as credible and convincing." *Id.*

DESC affirms that the factual showing made in Docket No. 2012-218-E remains accurate and relevant today. Incentive compensation expenses are a reasonable, necessary and prudent cost of operating DESC's system. For DESC to attract and retain qualified personnel, the Company's total compensation package must be competitive with the compensation packages offered by utilities and other businesses with whom the Company competes for personnel. Absent incentive compensation, DESC's compensation package would not be competitive, and the Company would have difficulty attracting and retaining skilled and qualified employees.

DESC acknowledges that in certain past proceedings, as a matter of necessary compromise, it has accepted a 50% reduction of recovery of incentive compensation through rates. However, DESC would respectfully show that the 50% disallowance is without reasonable basis and denies the utility the right to recover the full amount of its employee compensation expense.

Based upon DESC's incentive compensation being a reasonable, necessary and prudent cost of gas operations, DESC respectfully requests the Commission allow recovery of the $237,172 of costs associated with employee incentive pay. Furthermore, considering Order No. 2019-341 and Order No. 2019-323, the disallowance of these expenses is not consistent with the "pro-forma adjustments historically permitted or required by the commission . . . for similarly situated utilities." S.C. Code Ann. § 58-5-430.

3. Removal of Fifty Percent of the Base Pay and Benefits for Four Highest Executives Overseeing DESC's South Carolina Gas Operations

ORS recommends disallowing 50% of the base salary and benefits paid to four executives overseeing DESC's South Carolina gas operations. Specifically, the Report

> recommends an adjustment of ($329,783) to remove fifty percent (50%) of the base pay and benefits paid to the Company's four (4) highest compensated executives allocated to the Company's South Carolina natural gas operations. These four (4) executives' job duties are solely focused on increasing value for the Company's shareholders and provide no discernable additional benefit to the Company's customers.

ORS Report at 4-5.

The four executives in question are Felicia Howard, D. Russell ("Rusty") Harris, Shaun Randall, and Cedric Green.[2] During the relevant time period, each of these employees worked in the gas area with responsibility for matters directly benefitting customers, specifically safety, system integrity, reliability, gas supply and dispatch, customer service and sales:

a. Felicia Howard is an engineer with oversight responsibility for the daily operations of DESC's natural gas distribution system, including maintenance, construction, and gas sales. She is responsible for the overall reliability of the DESC gas distribution system, which includes ensuring that the system can provide safe and reliable service to customers. Her title is Vice President for Gas Operations for DESC.

b. Cedric Green is a PhD mechanical engineer who, during the relevant time period, was responsible for gas services for Dominion's Southeastern Gas Group, which includes DESC natural gas distribution system as well as systems in North Carolina. He is responsible for transmission and distribution pipeline integrity management (*i.e.*, inspections, maintenance, safety and repair programs); gas supply and asset management; central dispatch; gas control; measurement engineering/design and build; business development; transmission pipeline engineering/design and build; and the operation, safety and management of three liquefied natural gas plants, two of which serve customers of DESC. His title is Vice President, Gas Services, Southeast Energy Group.

c. Until October 2018, Shaun Randall, held the job that Mr. Green later filled. Mr. Randall is now responsible for Dominion's gas operations in North Carolina. The compensation expense that ORS disallowed for Mr. Randall was incurred prior to that transition. Mr. Randall's roles and responsibilities during that time were equivalent to Mr. Green's.

d. Rusty Harris, also an engineer, oversees and coordinates the work of Felicia Howard, Cedric Green, Shaun Randall and other executives responsible for DESC

[2] The identities of the four executives in question were not previously disclosed to ORS but their compensation information was provided by employee id number as the executives with the highest amount of compensation allocated to natural gas operations. Considering the importance of this matter, the Company has decided to disclose the details of their job descriptions and their identities in this filing.

> gas operations. He also has responsibility for customer service operations for Dominion Energy's Southeast Energy Group and reports to DESC's President, Rodney Bevins, for all matters related to those operations. His title is Vice President and General Manager, Gas Operations, Southeast Energy Group.

Those executives were located in South Carolina during the relevant parts of the review period. All had direct responsibility for DESC's gas systems and service to customers during the relevant period.

DESC would respectfully submit that there is no basis to conclude as to these four executives that their "job duties are solely focused on increasing value for the Company's shareholders and provide no discernible additional benefit to the Company's customers." Report at 4. In fact, something much closer to the opposite is true. The job duties of these executives were primarily if not entirely focused on safety, reliability and efficient operation of the gas system and on the quality of service provided to gas customers either in South Carolina or elsewhere on DESC's gas system. Their work provided direct and substantial benefits to the Company's gas customers. There is no factual basis to deny recovery of 50% of the cost of their services to DESC's gas distribution operations.

Furthermore, the recommended adjustment to disallow these costs is clearly not an "accounting and pro-forma adjustments historically permitted or required by the commission for the utility in question, . . . or authorized by general principles of utility accounting, or authorized by accounting letters or orders issued by the commission." S.C. Code Ann. § 58-5-430. Nor, given the nature of the work performed by these individuals, can this adjustment be determined to be analogous to the adjustment recognized for other utilities in recent orders. *Cf.*, Order No. 2019-341 and Order No. 2019-323 at 27, 56-57 (disallowing compensation to certain senior executives at the utilities' holding company level).

DESC respectfully requests the Commission allow recovery of the $329,783 of costs associated with these executives' pay and benefits.

ATTRIBUTING INCENTIVES TO CAPITAL PROJECTS

In the Report, ORS requests that the Commission require the Company to identify and provide the capitalized incentives and associated taxes included in plant-in-service, accumulated depreciation and depreciation expense in future RSA filings. ORS Report at 4-5. What ORS requests is not feasible for the reasons stated below.

DESC capitalizes the internal labor costs associated with capital projects or assets. It does so following Generally Accepted Accounting Principles ("GAAP") and the components of construction cost prescribed by the Federal Energy Regulatory Commission's ("FERC") Uniform System of Accounts ("USoA"). The number of accounting issues involved are massive. Capital projects or assets typically number in the tens of thousands each year (approximately 50,000 for DESC's gas distribution system in 2018).

The labor costs associated with each of those projects or assets properly include the costs of payroll, benefits, incentives and taxes as incurred during the year they are incurred. Within the Company's fixed asset ledger, incentive labor has not been tracked separately. Nor is it practical to do so going forward given the fact that capital costs are allocated across multiple assets and these asset accounts often have different depreciation rates and depreciation histories.

As improvement work or betterment work is done to capital assets, the new costs are booked to the appropriate capital asset account. Capital assets may remain on the books for 40 years or more as they are depreciated over their useful lives. Useful lives may be extended due to new investment or betterment of the asset. Therefore, many vintages of cost may be combined in the balance of the capital cost account for a single asset or class of assets, ultimately leading to varying levels of accumulated depreciation for each vintage. Furthermore, over the many decades of accumulating costs that comprise the Company's current fixed assets, the Company has converted from paper records to automated systems and the level of detail converted to the automated systems was at times summarized with the details maintained in the paper records.

In the Report, ORS requests that the Commission require the Company in future RSA filings to identify and separately itemize the incentive portion of labor costs and associated taxes included in plant-in-service *(i.e.,* the utility capital accounts used in setting rates), and the associated accumulated depreciation and depreciation expense. ORS Report at 4-5. DESC has explained to ORS that, for the reasons stated above, it is not practical to identify the capitalized incentives and associated taxes that are included in current plant-in-service, accumulated depreciation and depreciation expense. DESC's capital accounts have been maintained in full compliance with GAAP and the FERC USoA, but they do not permit incentive-related labor costs, which may stretch back over 40 years or more, to be differentiated from other capital costs as ORS requests. DESC respectfully requests that the Commission deny ORS's request.

TAX CUTS AND JOBS ACT RIDER

The tariffs set forth in Exhibit B of the Company's RSA filing include a tax reform rate rider ("tax rider") for the refund of income tax amounts charged through customer rates related to the effects of the Tax Cuts and Jobs Act and deferred in a regulatory liability during the review period. In addition, the tax rider includes the refund of amounts deferred related to the re-measurement of federal deferred income taxes. The amount the Company proposes to refund to firm customers through the tax rider beginning with the first billing cycle in November 2019 is $5,336,773. The tax rider will expire after the last billing cycle of October 2020. ORS did not propose any adjustments to the amounts calculated by the Company. DESC respectfully requests that the Commission approve the proposed tax rider.

CONCLUSION

For the reasons stated herein, DESC requests that the Commission allow recovery through rates of 1) amounts related to economic development expenses; 2) 100% of employee incentive pay; and 3) 100% of the base pay and benefits paid to the Company's four highest compensated executives allocated to the Company's South Carolina natural gas operations, totaling $601,456. DESC also requests the Commission deny ORS's request that the Company separately state incentive labor costs embedded in capital accounts and related items in future filings and that the Commission authorize the Tax Cut and Jobs Act Rider as proposed.

By: Matthew W. Gissendanner

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Attorneys for Dominion Energy South Carolina, Inc.

Date: September 13, 2019

BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2019-6-G

IN RE:

Dominion Energy South Carolina, Inc.'s Filing of Quarterly Monitoring Report for the twelve-month period ending March 31, 2019, and Proposed Rate Adjustments Pursuant to the Natural Gas Rate Stabilization Act	)	**CERTIFICATE OF SERVICE**

This is the certify that I have caused to be served this day one (1) copy of Dominion Energy South Carolina, Inc.'s **Response to the South Carolina Office of Regulatory Staff's Review of DESC's Gas Rate Stabilization Act Monitoring Report** to the persons named below at the addresses set forth via electronic mail and U.S. First Class Mail:

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Karen M. Scruggs

Karen M. Scruggs

Cayce, South Carolina

This 13th day of September, 2019